No. 12961

# In the United States Court of Appeals for the Ninth Circuit

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UNITED STATES OF AMERICA, APPELLANT

*v.*

ADAMANT COMPANY, WALTER B. SCOVILLE, JOE SEEPLE, HARRY WYNN, HERSCHEL BULLEN, MARY N. BULLEN, J. C. HAYWARD AND MARY S. HAYWARD; RECONSTRUCTION FINANCE CORPORATION, AS ASSIGNEE OF TREASURE COMPANY, APPELLEES

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UNITED STATES OF AMERICA, FOR THE USE OF RECONSTRUCTION FINANCE CORPORATION, A FEDERAL CORPORATION, ACTING IN BEHALF OF DEFENSE PLANT CORPORATION, A FEDERAL CORPORATION, APPELLANT

*v.*

ADAMANT COMPANY, WALTER B. SCOVILLE, JOE SEEPLE, HARRY WYNN, HERSCHEL BULLEN, MARY N. BULLEN, J. C. HAYWARD AND MARY S. HAYWARD, APPELLEES

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*UPON APPEAL FROM THE UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF CALIFORNIA, CENTRAL DIVISION*

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## BRIEF FOR THE UNITED STATES, APPELLANT

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*UPON APPEAL FROM THE UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF CALIFORNIA, CENTRAL DIVISION*

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## BRIEF FOR THE UNITED STATES, APPELLANT

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### JURISDICTION

This is a suit by the United States to condemn land in Los Angeles, California, under authority of section

5d (5) of the Reconstruction Finance Corporation Act of January 22, 1932, c. 8, 47 Stat. 5, as added by the Act of March 27, 1942, c. 198, 56 Stat. 174, 15 U. S. C. sec. 606b (5), and Title II of the Second War Powers Act of March 27, 1942, c. 199, sec. 201, 56 Stat. 176, 177, 50 U. S. C. App. sec. 632, as extended by Executive Order 9217, August 7, 1942, 7 F. R. 6177, 50 U. S. C. App. following sec. 632. The district court had jurisdiction under Title II of the Second War Powers Act, *supra,* and section 1 of the General Condemnation Act of August 1, 1888, c. 728, 25 Stat. 357, 40 U. S. C. sec. 257. The judgment appealed from was entered on October 30, 1950 (R. 154–156). A motion by the United States to vacate and set aside findings and judgment was denied on December 11, 1950 (R. 183–184).[1] A notice of appeal was filed by the United States on January 2, 1951 (R. 185–186). A notice of appeal was also filed by the United States on January 5, 1951, for the use of Reconstruction Finance Corporation (R. 187). This Court has jurisdiction of the appeal under 28 U. S. C. section 1291.

## QUESTION PRESENTED

Where a lessee acquires oil and gas leases on two contiguous tracts to make a minimum drill site of one acre, where under local law only one well could be and was drilled on such combined site, where both sides offered testimony only as to the value of the "total working interests" in the well, and where such testimony reflected the value of the lessee's interest in

[1] Similar motions filed by the other parties in this case were likewise denied on that date (R. 183–184).

the total estimated future production of the well at the time of taking by the Government, does an award for such value in a condemnation proceeding compensate the lessee for its interest in both leases?

## STATEMENT

This is a condemnation proceeding instituted on September 28, 1942, by the United States, for the use of Reconstruction Finance Corporation, acting in behalf of its subsidiary Defense Plant Corporation[2] to condemn real property in the City of Los Angeles, California. The property, consisting of a largely depleted oil field known as the Playa del Rey Field, was taken for use as a natural gas reservoir.[3] While many different parcels were within the area condemned, this appeal involves two contiguous tracts on which Treasure Company owned oil and gas leases. Those leases are known as the Fletcher lease and Burns No. 1 lease. The former consists of lots 9, 10 and 11, Block 33, Tract 9809, while the Burns No. 1 lease consists of lots 7, 8, 35 and 36 in Block 33, Tract 9809 (Fdg. I, R. 135).[4] The areas covered by these leases are identified in color on Plaintiff's Exhibit 1, Original, the Fletcher lease being colored in solid orange, while the Burns No. 1 lease is cross-hatched in brown. An

[2] This corporation was merged with the Reconstruction Finance Corporation by the Act of June 30, 1945, 59 Stat. 310.

[3] Other cases arising out of this proceeding were before this Court in *United States* v. *Block*, 160 F. 2d 604 (1947) and *Treasure Company* v. *United States*, 169 F. 2d 437 (1948).

[4] The lots constituting the Fletcher lease were described in the complaint as Parcel No. 251, while the lots in the Burns No. 1 lease are described in the complaint under Parcels 247, 249 and 250 (R. 8–9).

oil well identified as Treasure Well No. 8 was drilled on lot 9 of the Fletcher lease (Fdg. II, R. 136).

In its answer defendant Treasure Company alleged its ownership of the Fletcher lease and the Burns No. 1 lease (paragraphs V and VI, R. 44, 46). It also alleged ownership of two other oil and gas leases known as Burns No. 2 and Burns No. 3 leases, and alleged a value for its Fletcher lease as of September 28, 1942, of $1,000,000.00 and a like value for the three Burns leases combined (paragraphs VII, VIII, X and XI, R. 47, 48, 49).[5]

Defendant Adamant Company alleged ownership, through an agreement with Treasure Company, of a 25% participating interest in the Burns No. 1 and Fletcher leases and in Treasure Well No. 8 and that "Treasure Well is located upon the drill-site composed of the two above [Fletcher and Burns No. 1] leaseholds," (Ans., paragraphs IV and V, R. 15–16). It was further alleged that Adamant Company had drilling rights also in Burns No. 2 and Burns No. 3 leases, and alleged a value for all of such interests of $300,000.00 (Ans., paragraphs VI and VIII, R. 17–18).

Similarly defendant Scoville alleged an interest of 17% in the Fletcher and Burns No. 1 leaseholds, under the same agreement with Treasure Company, and valued his interest at $204,000 (Ans., paragraphs I, III, R. 20–21). Defendant Wynn likewise alleged ownership of a 5% interest in the Fletcher and Burns No. 1 leases and in Treasure Well No. 8, having a

[5] As will hereinafter appear, the Burns No. 2 and Burns No. 3 leases are not involved on this appeal.

value of $60,000.00 (Ans., paragraphs II and III, R. 22). Defendants Herschel Bullen and Mary H. Bullen alleged ownership of a 1% interest in oil production from the Fletcher lease, as did defendants J. C. Hayward and Marion S. Hayward, and asked the court to determine the value of such interest (Ans., R. 53–55). Defendant C. F. Johnson claimed a 2½% interest in the Fletcher and Burns No. 1 leases here involved as well as in Burns leases 2 and 3 not here involved and that all those interests had a value of $50,000.00 on the date of the taking (Ans., R. 31–35).[6]

Trial proceedings were had before Judge Beaumont and a jury, beginning on April 19, 1949, as to the value of the Fletcher and Burns No. 1 leases among other parcels (Fdg. VI, R. 137; R. 210–1187). During the course of the trial the Government settled with the landowners or lessors under those two leases (Fdg. VII, R. 138, 1165). Hence the only interest in those leases before the jury at the valuation trial was the lessee's interest.

At the valuation trial neither the Government nor any of the defendants[7] offered any testimony as to a value for the lessee's interest in either the Fletcher or Burns No. 1 lease separately. The testimony offered by all parties was as to the value of the lessee

[6] Johnson's claim was settled during the trial (R. 437–438).

[7] At the time the trial began, the Government was negotiating for settlement of Treasure Company's claim. Treasure Company assigned its interest to the Reconstruction Finance Corporation (Fdg. XXIII, R. 145) and that defendant did not participate in the valuation trial.

interest in Treasure Well No. 8.[8] Similarly, the form of verdict approved by all parties and placed before the jury did not include as items the lessee interest in either of the two leases, but did include as an item the following: "H–I W. I. Being the total working interest in Treasure Company Well No. 8" (R. 65). And the sole question on this appeal is whether an award for that item covers the lessee interest in both of those leases or only the lessee interest in the Fletcher lease on which the well was drilled.

The testimonial record of the valuation trial is lengthy, but may be summarized as follows. The Government's first expert witness was Mr. John F. Dodge, during whose appearance on the stand the symbol H–I W. I., or working interest, was developed and its meaning fixed. This witness used what was described as the decline curve method of estimating future production of the well, the rate of recovery and the future operating costs (R. 241, 340).[9]

Proper understanding of the testimony of this witness as to the working interests in Treasure Well No. 8 requires notice of the pattern followed by him in testifying previously as to other parcels. He explained that a community lease is one where a number

[8] The various defendants of course had claims to percentages of such value under alleged contracts with the lessee, Treasure Company. But the distribution of the award, as between these claimants, was not placed before the jury (R. 1073). Distribution was later ordered by Judge Westover in proceedings which gave rise to this appeal (R. 154).

[9] The technical details of the process by which this witness or any other witness arrived at his opinion of value is not of great importance now.

of individual lot owners get together and join in a lease to a single oil and gas lessee and that the lessee in turn may sublet a portion of the land to various oil companies, or all of the land to one such operator; that such subleases under a community lease were marked on Plaintiff's Exhibit 1, Original, by cross-hatching in color (R. 228–229). He further explained that the royalty payable to the landowners under a community lease was commonly 16⅔% (R. 231). He then explained that the lessee under the community lease, when he subleased to another would ordinarily reserve a total royalty greater than that which he must pay the landowners, and that the difference between the two was called an overriding royalty. He then proceeded to value various community leases on the basis of landowners' royalty and overriding royalty (R. 232–233). A uniform pattern was adopted of giving to the landowners' royalty under a community lease a designation by letter as, for example, "Parcel A" which was Herndon Community Lease No. 1 (R. 251). The overriding royalties under subleases under that community lease were given the designations A–1 (R. 257), A–2 (R. 259) and A–3 (R. 261). That procedure was adhered to also in valuing the other community leases which were involved.

Burns acquired his interest in the lots here involved under a sublease from the holder of the Herndon Lease West of Falmouth Avenue (R. 283, 286, 718, Adams, Scoville and Wynn Ex. G, Original). Herndon Lease West of Falmouth Avenue was desig-

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nated as "Parcel G" (R. 283). The witness Dodge gave for Parcel G, the landowners' royalty, a value of $40,340.00 and proceeded to value the overriding royalties on two subleases given designations G–1 and G–2 (R. 284–285). The sublease from Herndon to Burns was called "G–3" and the witness explained that these four lots were joined to the Fletcher lease to comprise a one-acre drill site. In response to a question by the Court the witness testified that the seven lots (three in the Fletcher lease and four in the Burns lease) comprise "the necessary legal one-acre in order that a well be drilled" (R. 286). The witness went on to testify that since the Burns lease called for only a 12.03% royalty, there was no overriding royalty and that the 12.03% had been included in the figure he had previously given, $40,340, as Parcel G, the landowners' royalty for the whole of Herndon Lease West of Falmouth Avenue, and thereupon G–3 was eliminated as a separate parcel. "In this instance, by a special arrangement, specially executed lease, these lots were joined to the parcel known as the Fletcher Lease and called for a 12.03% royalty. So it accrues to the lot owners in Parcel G" (R. 286–287).

The Fletcher lease was given the symbol H (R. 287). The witness testified that Treasure Well No. 8 was drilled on the Fletcher lease, but that it was also subject to the royalty interest of 12.03% royalty on the Burns lease which he had previously described as payable to the lot owners in Herndon Community Lease West of Falmouth. He was then asked what was his opinion of the value of the "working interest"

in Treasure Well No. 8, and the witness stated (R. 306): "The total working interest in the Treasure No. 8 well under conditions of total royalty as disclosed by the title search is $150,830. That title search discloses the well as subject to a total of 28 7/10ths per cent royalty and the value which I have given for the total working interest is predicated upon that royalty being paid." The 28 7/10 per cent royalty was broken down by the witness as "being 16 6/7 per cent to the Fletcher lease and 12.03 per cent to the Herndon Community west of Falmouth" (R. 307).[10] The 12.03%, as already detailed, was the royalty payable on the Burns lease. The witness then stated that "I have placed upon the map [Plaintiff's Exhibit 1, Original] the symbol H–I Working Interest, to designate the value which I have given as the working interest in the Well Treasure 8 located on Parcel H" (R. 307). It was later established that the symbol H-I W. I. was used to designate the total working interest, and the symbol H-I was adopted to designate the total or combined landowners' royalty (R. 399, 400). Working interest included all interests in the well "excluding only the two landholders' royalties, the one to Fletcher and the one to the Herndon Community Lease West of Falmouth" [the Burns lease]. "It

[10] As hereinafter detailed, the parties subsequently agreed that the royalty actually called for by the Fletcher lease was 7.365%, and that the combined royalties (7.365% to Fletcher and 12.03% to Burns) were 19.395% which they agreed to shorten to 19.4%. They so stipulated (R. 746) and as a result the expert witnesses of both the Government and the defendants were recalled to testify on that basis.

[the well] was drilled on the Fletcher, but pays a royalty not only to the Fletcher but to the adjoining lots [the Burns lease] which I have previously described, that 12.03 per cent royalty going to the lot owners in Parcel G" (R. 307–308). In response to a question by defendant Johnson, claimant of an interest,[11] the witness testified "I have stated, Mr. Johnson, that was after the landowners' royalties, the 12.03 and the 16.67 per cent were taken out. In other words, it is the profits to the operators of the well" (R. 309). Likewise he testified that the working interest "amounts to the difference between 100 per cent and 28 7/10 per cent, or 71.3 per cent *of the production*" (italics supplied (R. 309–310)). Similarly, on cross-examination he testified that his figure of $150,830 represented the value of all the working interests, and is based upon a 17-year life, a total future recovery of 344,800 barrels of oil, and the accompanying gas and gasoline, and that it represented 71.3 per cent of the oil. At this point the witness gave a value of $71,440 for the 28.7 per cent combined landowners' royalty (R. 333).[12]

The Government's other expert witness was Mr. Harry P. Stolz. He testified that past production performance of an oil well can be projected into the future and the future production thus estimated

[11] Johnson's claim was later settled by the plaintiff during the trial (R. 437–438).

[12] The witness explained that the production expenses came out of the working interest (R. 333–334). This explains why the figure of $150,830.00 for the working interest does not bear the exact ratio to the $71,440.00 for the landowners' royalty as 71.3 to 28.7.

(R. 385). His primary factor was the past production performance of the well (R. 388). This is the decline curve method used by the witness Dodge. He used the same basic data as had Dodge, but arrived at his valuations independently (R. 391). Stolz, however, arrived at generally lower values for the various landowners' royalties, and for overriding royalties under subleases than did the witness Dodge. This was likewise true when it came to evaluating the H–I W. I. working interest in Treasure Well No. 8. He testified that Treasure Well No. 8, marked H–I W. I. on Plaintiff's Exhibit 1, Original, had a working interest of 17.30 per cent [*sic,* obviously an inadvertent error of either the witness or the reporter, and intended to be 71.30, 100% less the combined landowners' royalty of 28.7%] and that he valued such working interest at $97,029 (R. 397). He valued the combined landowners' royalty of 28.7% at $57,838 (R. 401).[13]

The valuation testimony introduced by the defendants initially differed from that of the Government in that it was addressed to the total mineral value of the well Treasure No. 8. Defendant Seeple, who claimed a 17% interest under an agreement with Treasure Company (R. 483), testified that Treasure Well No. 8 had a market value of one million to two million dollars (R. 465).

[13] At this point it was discovered that no symbol had been adopted to designate the combined landowners' royalty, and H–I was used to distinguish this combined royalty from H–I W. I., the total working interest (R. 399–400). As hereinbefore noted (p. 5, *supra*), the *value* of the combined landowners' royalty was settled as between the landowners and the Government.

Defendant's chief expert witness was Dr. Robin Willis. The witness testified that he had been called to evaluate Treasure Well No. 8 "as a producing well in terms of dollars and cents" (R. 537). He further testified that there are two methods of estimating the oil that can be produced in the future, one the decline curve method based on past production (which was the approach of the Government expert witnesses), and the other method based upon estimating the area from which the well will produce oil, the sand thickness and other factors (R. 538–539). The witness considered the decline curve method was unreliable as to Treasure Well No. 8 (R. 540) and preferred the other method, which he labeled the volumetric basis (R. 545). On the latter basis he estimated that the recoverable oil amounted to 1,964,400 barrels (R. 555) and on his assumption that no additional wells could be drilled within that portion of his drainage area of 32.2 acres which lay west of Delgany Avenue, which was about half of his estimated drainage area (R. 588–592), he testified that "the total mineral interests, including landowners' and working interests", had a value of $1,251,000.00 (R. 606). Assuming that three additional wells might be drilled by other parties west of Delgany Avenue, he testified that the valuation of $1,251,000.00 for the total mineral interest would be reduced 30% and gave a valuation on this basis of $875,000.00 (R. 607). Both the $1,251,000.00 and the $875,000.00 figures were based on the volumetric method of estimating future production (R. 608). Apparently unwilling to gamble alone on this method, the defendants proceeded to have the witness testify

on the basis of two decline curves, the method which had been used by the Government witnesses (R. 608). On the basis of a decline curve which the witness had prepared (designated on Adamant, Scoville and Wynn Exhibit Q as "Willis-B"), the witness valued "the total market value of the leasehold as of September 28, 1942" at $713,300.00 (R. 611). The witness later conceded he had miscalculated and reduced his valuation on the basis of decline curve Willis-B to $566,400.00 (R. 626). He testified on the basis of still another decline curve identified on said Exhibit Q as "Willis-D", to a valuation of $322,000.00 "for the total leasehold." (R. 612) Here again this witness later conceded error and reduced the valuation on the basis of Willis-D decline curve to $260,000.00 (R. 670). To recapitulate, this witness testified that the total value of the well, including both landowners' royalties and working interests, on the volumetric basis, was $1,251,000.00 assuming forbidden drilling west of Delgany Avenue, $875,000.00 if it be assumed three wells could be drilled in that area, $566,400.00 on the basis of Willis-B decline curve, and $260,000.00 on the basis of the Willis-D curve.

Defendant Wynn was allowed to testify as an owner. He claimed a 6% interest in Treasure Well No. 8 (R. 700) and testified merely that his interest, as of the date of taking, was worth $5,000 a per cent (R. 704).[14]

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[14] While Wynn's testimony did not go to the entire value of the well, on his per cent valuation that value would have been $500,000.00.

A difficulty lay in the fact that the Government's witnesses had testified to the value of the working interests while the defendants' testimony went to the total value of the well, a fact noted by the trial court (R. 667). There was also uncertainty as to the exact royalty payable to Fletcher under his lease to Treasure Company and hence as to the accuracy of the combined royalty figure of 28.7% used by the Government witnesses. This was finally straightened out by agreement of counsel that the Fletcher royalty was 7.365%, the Burns royalty 12.03%, and the parties stipulated that the true combined royalty was 19.4%. The trial court so ruled and stated that "we will have to introduce evidence on that basis" (R. 746).

Accordingly the Government recalled the witness Stolz who, on the basis of a combined landowners' royalty of 19.4% instead of 28.7%, increased his valuation for the "total working interest" to $126,500.00 (R. 758).

Likewise, Government witness Dodge was recalled and, on the basis of a 19.4% combined landowners' royalty, increased his valuation of "the total working interest" to $176,314.00 (R. 779).

The defendants recalled their chief valuation witness Willis to break down his various valuations of the total mineral interests in Treasure Well No. 8 and to evaluate the total working interest in the well on the basis of a combined landowners' royalty of 19.4%. Thus, on the basis of his total value of $1,251,000.00 on the volumetric basis and assuming no other drilling, he valued the working interests at

$976,000, taking the working interests as 80% (R. 869). On the basis of his figure of $875,700 for the total mineral interests, on the volumetric basis and assuming three other wells might be drilled, he valued the working interests at $683,200.00 (R. 870). On the basis of his Willis-B decline curve, under which he had previously valued the total mineral interest at $566,400 (R. 626), he valued the working interests at $440,880.00 (R. 871). Counsel for the defendants stated that he was not interested in having the witness value the working interests on the basis of the $260,000.00 total mineral interest value the witness had previously given the jury on the basis of his Willis-D decline curve (R. 872). However, on cross-examination the witness testified that, on the basis of his $260,000.00 valuation of the total mineral interests, based on his Willis-D decline curve, the total working interests, figured on the lower combined royalty of 19.4% (he used 20% for convenience), were of a value of $194,500.00 (R. 885). Thus, in the final analysis, the various alternatives presented to the jury were the following valuations of the total working interests:[15]

| | |
|---|---|
| Government witness Stolz | $126,500.00 |
| Government witness Dodge | 176,314.00 |
| Defendants' witness Willis | 976,000.00 |
| Defendants' witness Willis | 683,200.00 |
| Defendants' witness Willis | 440,880.00 |
| Defendants' witness Willis | 194,500.00 |

[15] The valuations of one to two million dollars for the entire interests in the well by the witness Seeple and the apparent valuation of $500,000.00 for the entire interests by Wynn on the basis of his percent value of $5,000.00 were not specifically withdrawn. Nevertheless, those witnesses were not recalled to break down their

The case was given to the jury under an instruction that "your verdict as to the parcel designated 'H–I W. I.' must be predicated on the assumption that the royalty payable from the production of Treasure No. 8 Well is 19.4 per cent and not 28.7 per cent" (R. 1165) and the jury returned a verdict for "H–I W. I.—Being the total working interests in Treasure Company Well No. 8" in the sum of $194,500.00 (R. 65).[16] Judgment was entered accordingly on July 13, 1949, and no appeal was taken therefrom (R. 67–76).

On May 11, 1950, proceedings were had before Judge Westover for the purpose of determining distribution of the award. (R. 1188–1244). On October 30, 1950, the court filed its findings of fact and conclusions of law (R. 134–153) and on the same date entered judgment in accordance therewith. The court found, *inter alia,* that the Fletcher lease was referred to in the valuation trial as H–I W.I, and that the verdict fixed the value of the leasehold in the property on which Treasure Well was drilled and that the award was not made for oil to be produced, saved

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valuations to a total working interest valuation based upon a 19.4% combined landowners' royalty. Moreover, under the instruction of the court, those valuations would have had to be reduced by the percentage of 19.4%. The verdict of $194,500.00 for the working interests makes plain that the jury placed no reliance on these witnesses. Since the verdict was in the exact amount testified to by defendants' witness Willis on the basis of his Willis-D decline curve, it seems probable that the jury accepted defendants' lowest figure on the only method of estimating future production adopted by both sides, the decline curve method.

[16] As hereinbefore shown (p. 14, *supra*) this total royalty of 19.4% was a combined landowners' royalty, being made up of 7.365% payable to the landowner under the Fletcher lease, and 12.03% payable to the landowner under Burns No. 1 lease.

and sold from the leasehold nor was it limited to the value of Treasure Well No. 8 (Fdg. IX, R. 138); that H–I W.I. was indicated on the map, Plaintiff's Exhibit 1, original, as referring to the Fletcher lease and that Burns No. 1 lease was marked on the map as G–3 (Fdg. X, R. 139); that in findings of fact, conclusions of law, and the judgment in a California state case brought by Scoville, Seeple, Wynn and Adamant against Treasure Company and G. de Bretteville, the well was referred to as being on the Fletcher lease (Fdg. XIII, R. 140); that the jury's verdict of $194,500.00 established the value of the lessee's interest in the Fletcher lease (Fdg. XV, R. 140); that the leasehold containing the well Treasure No. 8 is the leasehold of the Fletcher lease and does not include the Burns No. 1 lease (Fdg. XIV, R. 140); that the verdict fixed the value of the Fletcher leasehold upon which the well was drilled (Fdg. XXXV, R. 149–150). The court concluded that the award of $194,500.00 was not for oil, but was for the value of the leasehold on which Treasure Well No. 8 was drilled and that the well was only a part of the leasehold interests (Concl. II, R. 150–151).

Since it is clear that under these findings the judgment based thereon stands as an adjudication that the United States has not paid for the Burns No. 1 leasehold, thus exposing the Government to this further liability, the Government filed a motion to vacate those findings (R. 174–181) and requested substitute findings to the effect that in the jury trial the lessee interest in both the Fletcher lease, covering lots 9, 10, and 11 in Block 33 and in the Burns No. 1 lease, cov-

ering lots 7, 8, 35, and 36 in Block 33, was described as the working interest and was designated "H–I W.I" and that the verdict fixed the value of the lessee interest, i. e., the working interest, in the property on which the well was produced (Requested fdg. A, R. 177); that the Fletcher and Burns No. 1 leases were combined to make a minimum drill site of one acre, on which Treasure Well No. 8 was completed and produced (Requested fdg. B, R. 177); and that the lessee interest in such leasehold estate, designated H–I W. I. in the testimony and jury verdict was by stipulation of counsel, adopted by the court, agreed to be subject only to an aggregate landowners' royalty of 19.395%, of which 7.365% was payable as the Fletcher lease and 12.03% was payable on the Burns No. 1 lease, and that for purposes of the testimony and computations of witnesses it was agreed by counsel that such combined landowners' royalty of 19.395% could be called 19.4% (Requested fdg. C. R. 178).

That motion was denied on December 11, 1950 (R. 183–184), and this appeal followed.

## SPECIFICATION OF ERRORS

The statement of points relied on by the United States on its appeal (R. 203–206), adopted in this Court (R. 1266), may be summarized as follows:

The district court erred:

(1) In refusing to vacate the judgment entered October 30, 1950, and in refusing to vacate findings IX, X, XIII, XIV, XV, and XXXV upon which the judgment was based, and in refusing to make substitute findings A, B, and C as requested by appellant.

(2) In finding and concluding that the award of $194,500.00 for "H–I W. I., being the total working interest in Treasure Company Well No. 8," represented the value of the lessee's interest in the Fletcher leasehold, and that such award did not compensate for the lessee's interest in the Burns No. 1 lease.

(3) In refusing to hold that the Fletcher and Burns No. 1 leases were combined to make a minimum legal drill site of one acre, in refusing to hold that "H–I W. I., being the total working interests in Treasure Company Well No. 8," represented the value of the lessee interest in both of those leases, and in refusing to hold that the award of $194,500.00 for such total working interest compensated for the value of the lessee interest in both of such leases.

## ARGUMENT

Initially it is to be observed that the Government is not in this case subject to the usual heavy burden resting upon an appellant who seeks to overturn findings of fact. The question of whether the award of $194,500.00 covered the lessee interest in both the Fletcher and Burns leases is determined solely by the proceedings in the valuation trial. That trial was presided over by Judge Beaumont. The distribution proceeding was later conducted by Judge Westover. Hence this is not a case where he is peculiarly fitted to pass upon questions of fact by reason of having heard and observed witnesses while testifying. That function, even before Judge Beaumont, rested with the jury. The evidence upon which Judge Westover made his findings was wholly documentary, in the

form of the reporter's transcript of the trial proceedings and testimony, with the exhibits introduced by the parties.

In this situation several courts of appeals, including this one, have taken the view that when the evidence is all documentary the appellate court is in just as good a position as the trial court to appraise the evidence and hence the trial court findings do not carry great weight. *Equitable Life Assur. Soc.* v. *Irelan,* 123 F. 2d 462 (C. A. 9, 1941); *Bowles* v. *Carnegie-Illinois Steel Corp.,* 149 F. 2d 545 (C. A. 7, 1945); *British-American Assur. Co. of Toronto, Canada* v. *Bowen,* 134 F. 2d 256 (C. A. 10, 1943); *Himmel Bros. Co.* v. *Serrick Corporation,* 122 F. 2d 740 (C. A. 7, 1941); *Fleming* v. *Palmer,* 123 F. 2d 749 (C. A. 1, 1941); *State Farm Mut. Automobile Ins. Co.* v. *Bonacci,* 111 F. 2d 412 (C. A. 8, 1940).

I

*The award of $194,500.00 for "H–I W. I., being the total working interest in Treasure Well No. 8," represented the lessee interest in both the Fletcher and Burns No. 1 leases.*—The evidence placed before the jury in the valuation proceeding has already been carefully analyzed (*supra,* pp. 6–16) and it is unnecessary to repeat it here. It undeniably appears therefrom that the award for H–I W. I. actually represented the total economic value to the lessee of the future mineral production of the well. This is so because the jury was instructed in this connection to arrive at its verdict on the basis of there being payable to the landowners of the Fletcher and Burns leases

a combined royalty of 19.4% (R. 1165). And as hereinbefore unmistakenly shown, the evidence of both sides placed before the jury various opinions as to the mineral value of the well to the lessee after payment of 19.4% to the landowners.

The Fletcher and Burns No. 1 leases were *oil and gas leases,* not leases for other purposes. The jury was told very early in the trial by the witness Dodge that a drill site of one acre is required by state law (R. 269) and that the four lots comprising Burns No. 1 lease were combined with the three lots in the Fletcher lease to comprise a one-acre drilling site (R. 285–286). They were also informed by this witness that "That is a lease of one acre and no additional wells could be drilled on the lease within the law" (R. 350). That proposition was never questioned by the defendants and the entire case was tried on that basis. It was thus obvious to the jury that the mineral value of the entire one-acre drill site to the operating lessee, as to the lessors, lay in the only well which could be drilled thereon.

The fact that physically the well was drilled on the Fletcher lease is of no significance. An oil and gas lease on the Fletcher lease alone had absolutely no value since no well could be drilled. Obviously when both Fletcher and Burns executed oil and gas leases to Treasure Company for the express purpose of creating a minimum drill site, and with full knowledge that only one well could be drilled, the royalties reserved in the production of oil and gas in either lease were in no wise dependent upon whether the

well would physically be drilled on one or the other. On identical reasoning the value of the combined drill site to the lessee was likewise the future economic value of the well to the lessee, whether it be on one or the other lease. That the production of the one and only possible well represented production from both leases was recognized throughout the trial by both parties as shown by the fact that both sides recognized that the combined landowners' royalty of 19.4% (12.03% to Burns and 7.37% to Fletcher) had first to be deducted. If only the Fletcher leasehold was being valued, then the deduction of the Burns royalty was improper. The combined landowners' royalty of 19.4% and the total working interest of 81.6% were component parts of the same thing—the total mineral value of the well. And just as the 19.4% represented the interest of the landowners in both leases, so the remainder of the 100% mineral value, the 80.6% working interest represented the lessee's interest in both leases.

This explains why neither side sought to value either the Fletcher lease as a unit or the Burns lease as a unit. The plain fact was recognized by both sides that, so far as the lessee was concerned, the lessee's interest in both leases was a unitary interest in the only well that could be drilled on the combined leases.

That for purposes of evaluating the working interest in Treasure Well No. 8 the combined leases as a unit were being valued is further shown by the record. Thus the Government witness Dodge, during

whose initial appearance on the stand the symbol H–I Working Interest was first developed, testified as follows: "That is *a lease of one acre* and no additional wells could be drilled on the lease within the law" [italics supplied] (R. 350). And again (R. 352–353), in discussing Johnson's Ex. A, he testified that "The first paragraph contains Lots 9, 10, and 11 and refer to the so-called Fletcher parcel which has been labeled H. The next paragraph includes Lots 7, 8, 35, and 36 and refers to the four additional lots which I believe have been labeled G–3, if I am not mistaken, * * * And those are the lots and comprise *the entire lease* upon which Treasure well was drilled." (Italics supplied.) Certainly this witness and the other Government witness who followed him were testifying to a lessee value in both leases, and the jury must have so understood it. And since defendants ultimately adopted the Government's approach, merely seeking to establish a higher value on the basis of larger estimates of future production, and never suggested that only the Fletcher lease was involved, it follows that the jury understood that their testimony also went to both leases.

That the defendants considered the combined leases as a single leasehold is conclusively shown by their Exhibit S, Original, which is a map in colors. As hereinbefore stated, in addition to the Burns No. 1 lease which was combined with the Fletcher lease to make Treasure Well No. 8 possible, there were also in the proceeding, but in no way involved here, two other leases known as Burns No. 2 and Burns No. 3.

During questioning by defendants of their witness Wynn regarding Adams, Scoville and Wynn Exhibit S, the following occurred (R. 697–698):

> Q. Did you mark on a map in colors the designation of *the Treasure well leasehold* and the two Burns leaseholds? [Italics supplied.]
>
> A. Yes, sir, I did.
>
> Q. I show you a map marked in red, purple, and green, and ask you if you made those markings?
>
> A. Yes, I did.
>
> * * * * *
>
> Q. (By Mr. ALLEN): Now will you step to the board here and point out the areas which you have marked? What is the purple area?
>
> * * * * *
>
> The WITNESS: The purple area consists of the one-acre drill site on which the Treasure well is now located. [Italics supplied.][17]

Thus, on defendants' own Exhibit S placed by them before the jury, Burns No. 1 lease was not considered by them as such but, coupled with the Fletcher lease, as comprising what defense counsel called "the Treasure well leasehold." The same thing is reflected in the answer of Adamant Co., Walter B. Scoville and Harry Wynn, where it is alleged "That Treasure Well No. 8 is located upon the drill-site composed of the two above leaseholds" [the Fletcher and Burns No. 1 leasehold] (R. 16). See also the same allegations by Adamant Company in its two separate petitions for partial distribution (R. 26, 58),

[17] Reference to Exhibit S shows the purple area as comprising all seven lots of the Fletcher and Burns No. 1 leases.

and in the answer of defendant C. F. Johnson (R. 33).

The district judge in the distribution proceeding misconstrued the symbols "H–I W. I." and "G. 3." In Finding IX it is stated that "the Fletcher lease was referred to and described as 'H–I W. I.'." That is not so. The Fletcher lease was referred to as "H" (R. 287). But as already shown, "H–I W. I." was not a sublease or any interest in land, but a standard of valuation adopted by both sides. This is clearly shown by the testimony of the witness Dodge who first used it. In view of the multiplicity of letters and figures which were being placed on the map, Plaintiff's Ex. 1, Original, at the suggestion of the court it was agreed that the symbols would be placed up in the white portion above the area taken and linked to the location on the map by a line (R. 260). After Dodge stated that he had placed the symbol "H–I Working Interest to designate the *value* which he had given is the working interest in the well" (R. 307), the court observed: "Mr. Dodge, you have drawn the 'H–I' so that it comes down to that orange part there [obviously the Fletcher tract]; what did you intend?" The witness replied: "Draw it *to the well,* because it is only an interest in the profits of the well and does not attach to the land" (Italics supplied) (R. 308). Obviously the witness was using the symbol as representing the value of the well to the lessee on both leases and not as representing the Fletcher lease alone. Nowhere in the record did the defendants initimate any different understanding.

That the presence of the letter H, which had been used to designate the Fletcher lease, in no wise indicated that H–I W. I. was limited to the Fletcher lease is also otherwise shown. During examination of the witness Stolz regarding the value of the combined landowners' royalty interest, some confusion resulted from the fact that no symbol for that combined royalty had been used, and it was finally straightened out by using "H–I" for the combined royalty interest (R. 399), to distinguish it from the other component part of 100% value of the well, the total working interest. And just as all present, including the jury, understood that H–I covered the *lessor's or landowner's* interest in both leases, so H–I W. I. was understood as covering the lessee's interest in both of those two leases.

Similarly the court below erred when it stated that "The Burns No. 1 lease is marked on said map as 'G–3' " (Fdg. X, R. 139). As fully developed in the statement (*supra,* pp. 6–8) G–3, under the settled pattern employed, referred to any overriding royalty accruing to the holder of Herndon Lease West of Falmouth Avenue under the sublease from such holder to Burns, and the value of which was credited by Dodge to the landowners as part of their total landowners' royalty in excess of $40,000 under their lease to Herndon, since by reason of the low royalty there was no overriding royalty. Thus at R. 286–287, it is clearly demonstrated that G–3 did not represent the lessee Treasure Company's interest in the Burns No. 1 lease. The witness Dodge, in response to a question of the court testified that "G–3 represents

the landowner's royalty on four lots" and that it was included in "G". There being no overriding royalty, "G–3" was eliminated as a separate parcel.

We agree with the court below (Fdg. IX, R. 138; Concl. II, 150) that H–I W. I. was not an award for oil as such. It was an award for the two leases. The parties simply recognized that the estimated profits accruing to the lessee from the one well that could be drilled on the combined site was the only standard of value to be applied. No other evidence was introduced by either side.

Note should also be made of the trial court's conclusion "that said well was only a part of the leasehold interests." (Concl. II, R. 151.) If by that is meant that the leaseholds had a value for other purposes than the mineral production of the well, it too is answered by the record. During a discussion of proposed instructions to be given the jury, the Government objected to defendants' proposed Instructions 1, 3 and 5 on the ground that they suggested the use for purposes other than that for which the property was used, and that the extraction of oil and gas was the highest and best use and the only use defendants were permitted to put this property to under the lease (R. 963, 965). The court observed there had been no evidence directly to the point (R. 965). Defendants had in mind that the property could be given value on the basis of the use the Government was making of it, gas storage. Counsel for defendants finally agreed that there was no evidence of value for any use other than extraction of oil and gas and that "it [the instruction] is not applicable" (R. 967).

It was thus conceded that the standard of valuation on the basis of the potential value of the well reflected the whole value of the property to the lessee.

Finally, in their statement of points and authorities in support of their motion for new trial following the judgment here appealed from, defendants Adamant Company, Scoville, Seeple and Wynn stated (R. 159):

> The evidence is sufficient to establish the Finding No. XIV that "the Jury's verdict of $194,500.00 established the value of the lessee's interest in the Fletcher lease, Lots 9, 10 and 11, Block 33, Tract 9809, on which Treasure Well No. 8 was located," *and the evidence is also sufficient to establish the value of the lessee's interest in the entire leasehold, comprised of 7 lots, upon the grounds that the only value of the leasehold was the value of the working interests in Treasure Well No. 8 (except, of course, the landowners fee title and landowners royalty—which was withdrawn from the jury)*. [Italics supplied.]

There can be no clearer concession that the evidence of both parties as to a single value for those working interests, and the fixing of that value by the jury, embraced the lessee's interest in all seven lots, which are here again referred to by defendants as a single or "entire leasehold," and that payment of that amount compensated the lessee for its interest in both leases.

## CONCLUSION

For the reasons stated, the judgment below should be reversed and the cause remanded to the district court with instructions to make appropriate findings

to the effect that the award of $194,500.00 covered the lessee's interest in both the Fletcher and Burns No. 1 leases.

Respectfully submitted.

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